

CITY OF KNOXVILLE

KNOXVILLE, IOWA

MUNICIPAL WATER WORKS FUND

INDEPENDENT AUDITOR'S REPORTS

BASIC FINANCIAL STATEMENTS AND SUPPLEMENTARY INFORMATION

SCHEDULE OF FINDINGS

June 30, 2010

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CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND

WATER WORKS OFFICIALS

<u>Name</u>	<u>Title</u>	<u>Term Expires</u>
Merle Vickroy	Trustee - Chairman	April, 2015
Dwight Sommar	Trustee	April, 2011
Richard Randol	Trustee	April, 2013
Steve Inskeep	General Manager	Indefinite
Michael Lane	Attorney	Indefinite

## INDEPENDENT AUDITOR'S REPORT

To the Board of Trustees  
City of Knoxville Municipal Water Works Fund  
Knoxville, Iowa

We have audited the accompanying financial statements of the business type activities, each major fund and the aggregate remaining fund information of the City of Knoxville Municipal Water Works Fund, as of and for the year ended June 30, 2010, which collectively comprise the Water Work's basic financial statements listed in the table of contents. These financial statements are the responsibility of Water Work's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

As described in Note 1, these financial statements were prepared on the basis of cash receipts and disbursements, which is a comprehensive basis of accounting other than U.S. generally accepted accounting principles.

In our opinion, the financial statements referred to above presented fairly, in all material respects, the respective cash basis financial position of the business type activities, each major fund and the aggregate remaining fund information of the City of Knoxville Municipal Water Works Fund as of June 30, 2010, and the respective changes in cash basis financial position for the year then ended in conformity with the basis of accounting described in Note 1.

In accordance with Government Auditing Standards, we have also issued our report dated August 16, 2010 on our consideration of the Water Works internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting and compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards and should be considered in assessing the results of our audit.

The Water Works has not presented management's discussion and analysis which introduces the basic financial statements by presenting certain financial information as well as management's analytical insights on that information that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of the basic financial statements.

The budgetary comparison information on pages 16 through 17 is not a required part of the basic financial statements, but is supplementary information required by the Governmental Accounting Standards Board. We applied limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. We did not audit the information and express no opinion on it.

Knoxville, Iowa  
August 16, 2010

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
STATEMENT OF ACTIVITIES AND NET ASSETS – CASH BASIS  
As of and for the year ended June 30, 2010

	<u>Disbursements</u>	<u>Program Receipts Charges for Services</u>	<u>Net (Disbursements) Receipts</u>
Functions/Programs:			
Business-Type Activities:			
Water	\$ <u>1,261,946</u>	\$ <u>1,582,814</u>	\$ <u>320,868</u>
General receipts:			
Unrestricted investment earnings			1,650
Rents collected			22,340
Miscellaneous			<u>49,978</u>
Total general receipts			<u>73,968</u>
Change in cash basis net assets			394,836
Cash basis net assets beginning of year			<u>1,113,740</u>
Cash basis net assets end of year			\$ <u>1,508,576</u>
Cash basis net assets unrestricted			\$ <u>1,508,576</u>
See notes to financial statements.			

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
STATEMENT OF CASH TRANSACTIONS AND CHANGES IN CASH BALANCES  
PROPRIETARY FUND  
As of and for the year ended June 30, 2010

	Enterprise Fund <hr/> Water Operating Fund <hr/>
Operating receipts:	
Use of money and property:	
Rent	\$ <u>22,340</u>
Charges for services:	
Sale of water	1,466,649
Sewer collection fee	50,000
Penalty fees	6,261
Taps	150
Customer service	1,622
Sales tax collected	<u>58,132</u>
	<u>1,582,814</u>
Miscellaneous:	
Utility credit	11,960
Reimbursements	7,849
NSF check charges	1,920
Merchandise sales	17,244
Settlement	3,380
Disconnect notices and fees	<u>7,625</u>
	<u>49,978</u>
 Total operating receipts	 <u>1,655,132</u>

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
STATEMENT OF CASH TRANSACTIONS AND CHANGES IN CASH BALANCES  
PROPRIETARY FUND  
As of and for the year ended June 30, 2010

	Enterprise Fund <u>Water Operating Fund</u>
Operating disbursements:	
Business Type Activities:	
Administration:	
Salaries	\$ 79,000
Payroll taxes and IPERS	15,816
Employee insurance	75,135
Training and meetings	2,082
Analysis fees	1,860
Insurance	56,732
Audit fees	6,015
Publications	1,394
Maintenance contract	21,305
Memberships and fees	3,331
Engineering and consulting	500
Board annual fees	750
	<u>263,920</u>
Accounting and Collections:	
Salaries	77,408
Payroll taxes and IPERS	9,608
Office supplies	7,294
Utilities and telephone	2,279
Postage	21,250
Collection fees	142
Janitorial service	2,765
Maintenance	1,390
Sales tax remitted	57,222
Banking and collection fees	6,450
	<u>185,808</u>

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
STATEMENT OF CASH TRANSACTIONS AND CHANGES IN CASH BALANCES  
PROPRIETARY FUND  
As of and for the year ended June 30, 2010

	Enterprise Fund Water Operating Fund
Operating disbursements (continued):	
Business Type Activities (continued):	
Plant and operation distribution:	
Salaries	\$ 343,301
Payroll taxes and IPERS	42,602
Electricity and gas	85,616
Chemicals	63,597
Gasoline and fuel	8,906
Maintenance and supplies	43,243
Sand, rock, and gravel	26,502
Distribution maintenance	74,137
	<u>687,904</u>
Other:	
Capital distribution projects	57,131
Capital project maintenance	56,204
Capital outlay	10,979
	<u>124,314</u>
Total operating disbursements	<u>1,261,946</u>
Excess (deficiency) of operating receipts over (under) operating disbursements	<u>393,186</u>
Non-operating receipts:	
Interest on investments	<u>1,650</u>
Excess (deficiency) of receipts over (under) disbursements	394,836
Cash balance beginning of year	<u>1,113,740</u>
Cash balance end of year	\$ <u><u>1,508,576</u></u>
Cash basis fund balance unreserved	\$ <u><u>1,508,576</u></u>
See notes to financial statements.	



CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
COMBINING STATEMENT OF CASH TRANSACTIONS AND CHANGES IN CASH BALANCES  
AGENCY FUNDS  
Year Ended June 30, 2010

	<u>Customer Deposits</u>	<u>Sanitary Sewer</u>	<u>Total</u>
Receipts:			
Charges for services:			
Sanitary sewer receipts	\$ -	\$ 2,269,295	\$ 2,269,295
Miscellaneous:			
Customer deposits	12,650	-	12,650
Total receipts	<u>12,650</u>	<u>2,269,295</u>	<u>2,281,945</u>
Disbursements:			
Agency Remittances:			
Remittances to City	-	2,269,295	2,269,295
Customer deposits reimbursed	13,895	-	13,895
Total disbursements	<u>13,895</u>	<u>2,269,295</u>	<u>2,283,190</u>
Excess (deficiency) of receipts over (under) disbursements	(1,245)	-	(1,245)
Balance beginning of year	<u>39,449</u>	-	<u>39,449</u>
Balance end of year	<u>\$ 38,204</u>	<u>\$ -</u>	<u>\$ 38,204</u>

See notes to financial statements.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2010

Note 1. Summary of Significant Accounting Policies

The City of Knoxville Municipal Water Works Fund is an independent department and a component unit of the City of Knoxville. The Water Works operates under an appointed Board of Trustees. The Water Works Department provides water service to the residents of Knoxville, Iowa, located in Marion County.

A. Reporting Entity

For financial reporting purposes, the Municipal Water Works Funds of the City of Knoxville, Iowa, has included all funds, organizations, agencies, boards, commissions and authorities. The Water Works has also considered all potential component units for which it is financially accountable, and other organizations for which the nature and significance of their relationship with the Water Works, are such that exclusion would cause the Water Works financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body, and (1) the ability of the Water Works to impose its will on that organization or (2) the potential for the organization to provide specific benefits to, or impose specific financial burdens on the Water Works. These statements do not include any other City of Knoxville funds or transactions.

B. Basis of Presentation

Government-wide Financial Statements – The statement of activities and net assets cash basis reports information on all of the nonfiduciary activities of the primary government, the Water Works Fund, and any component units. For the most part, the effect of interfund activity has been removed from this financial statements. The statement demonstrates the degree to which the direct disbursements of a given function are offset by program receipts. Direct disbursements are those that are clearly identified with a specific function. Program receipts include 1) charges to customers or applicants who purchase, use or directly benefit from goods, services, or privileges provided by a given function and 2) grants and contributions that are restricted to meeting the operational or capital requirements of a particular function. Other items not properly included among program receipts are reported instead on general receipts.

Fund Financial Statements – Separate financial statements are provided for proprietary and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual proprietary funds are reported as separate columns in the fund financial statements.

The Water Works reports the following major proprietary fund:

The Enterprise, Water Operating Fund accounts for the operation and maintenance of the City's water system.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2010

Note 1. Summary of Significant Accounting Policies

B. Basis of Presentation (continued)

Additionally, the Water Works reports the following fund type:

Fiduciary Funds:

Agency Funds are utilized to account for monies and properties received and held by the Water Works in a trustee capacity as an agent for individuals, private organizations, certain jointly governed organizations, other governmental entities and/or other funds.

C. Basis of Accounting

The Municipal Water Works Fund maintains its financial records on the basis of cash receipts and disbursements and the financial statements of the Water Works are prepared on that basis. The cash basis of accounting does not give effect to accounts receivable, accounts payable and accrued items. Accordingly, the financial statements do not present the financial position and results of operations of the funds in accordance with U.S. generally accepted accounting principles.

Proprietary funds distinguish operating receipts and disbursements from non-operating items. Operating receipts and disbursements generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. All receipts and disbursements not meeting this definition are reported as non-operating receipts and disbursements.

D. Budgets and Budgetary Accounting

The budgetary comparison and related disclosures are reported as Required Supplementary Information.

Note 2. Cash and Pooled Investments

The Water Works's deposits at June 30, 2010 were entirely covered by Federal depository insurance, or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The Water Works is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Water Works's Trustees; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investments companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2010

Note 2. Cash and Pooled Investments (continued)

The Water Works investments at June 30, 2010 are as follows:

Type	Amortized Cost
Iowa Public Agency Investment Trust	\$ 1,445,876

The Water Works investments in the Iowa Public Agency Investment Trust are not subject to risk categorization and are valued at amortized cost pursuant of Rule 2a-7 under the Investment Company Act of 1940.

Note 3. Pension and Retirement Benefits

The Water Works contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by State statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa 50306-9117.

Plan members are required to contribute 4.30% of their annual salary and the Water Works is required to contribute 6.65% of annual covered payroll. Contribution requirements are established by State statute. The Water Works's contributions to IPERS for the years ended June 30, 2010, 2009, and 2008 were \$29,741, \$28,815, and \$26,199, respectively, equal to the required contributions for each year.

Note 4. Other Postemployment Benefits (OPEB)

Plan Description – The Water Works participates in a single-employer retiree benefit plan which provides medical/prescription drug benefits for retirees and their spouses. The Water Works has 8 active and 3 retired members in the plan. Participants must be age 55 or older at retirement.

The medical/prescription drug benefits are provided through a partially self-insured plan with Wellmark through the City of Knoxville. Retirees under age 65 pay the same premium for the medical/prescription drug benefits as active employees.

Funding Policy – The contribution requirements of plan members are established and may be amended by the City. The plan is funded by City contributions and is administered by Group Services, Inc. The City assumes liability for claims between \$250 and \$2,500 for single coverage and \$500 and \$5,000 for family coverage. Claims in excess of the deductible are insured through the purchase of insurance. The City currently finances the retiree benefit plan on a pay-as-you-go basis. The most recent active member monthly premiums for the City and plan members are \$469 for single coverage and \$1,245 for family coverage. The same monthly premiums apply to retirees. For the year ended June 30, 2010, the Water Works contributed \$62,943, retirees contributed \$10,750, and active plan members eligible for benefits contributed \$3,613 to the plan.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2010

Note 5.   Compensated Absences

Water Works's employees accumulate vacation for subsequent use or for payment upon termination, retirement or death. These accumulations are not recognized as expenditures by the Water Works until used or paid.

Water Works's employees accumulate sick leave hours for subsequent use. A percentage of the value of sick leave accrued at retirement will be applied to payment of health insurance premiums after retirement. The applicable amounts are 75% for employees hired prior to July 1, 1980 and 50% for employees hired after July 1, 1980.

One employee retired during the year ended June 30, 2010. Seventy-five percent of the value of accrued sick leave at retirement for that employee was \$35,954. This makes three retired employees and their balance is being used to pay the monthly health insurance premiums of the retired employees until such time as the balance has been used. The premiums paid for the year ended June 30, 2010 were \$10,750. The balance at June 30, 2010 is \$54,087.

The Water Work's maximum liability for unrecognized accrued employee benefits has been computed based on rates of pay as of June 30, 2010 and is as follows:

<u>Type of Benefits</u>	<u>Amount</u>
Vacation	\$ 38,088
Sick Leave	102,688
Comp Time	<u>318</u>
Total	<u>\$ 141,094</u>

Note 6.   Risk Management

The Water Works is a member in the Iowa Communities Assurance Pool, as allowed by Chapter 670.7 of the Code of Iowa. The Iowa Communities Assurance Pool (Pool) is a local government risk-sharing pool whose 634 members include various governmental entities throughout the State of Iowa. The Pool was formed in August 1986 for the purpose of managing and funding third-party liability claims against its members. The Pool provides coverage and protection in the following categories: general liability, automobile liability, automobile physical damage, public officials liability, property, inland marine, and boiler/machinery. There have been no reductions in insurance coverage from prior years.

Each member's annual casualty contributions to the Pool fund current operations and provide capital. Annual operating contributions are those amounts necessary to fund, on a cash basis, the Pool's general and administrative expenses, claims, claims expenses and reinsurance expenses due and payable in the current year, plus all or any portion of any deficiency in capital. Capital contributions are made during the first six years of membership and are maintained to equal 200 percent of the total current members' basis rates or to comply with the requirements of any applicable regulatory authority having jurisdiction over the Pool.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2010

Note 6. Risk Management (continued)

The Pool also provides property coverage. Members who elect such coverage make annual operating contributions which are necessary to fund, on a cash basis, the Pool's general and administrative expenses and reinsurance premiums, all of which are due and payable in the current year, plus all or any portion of any deficiency in capital. Any year-end operating surplus is transferred to capital. Deficiencies in operations are offset by transfers from capital and, if insufficient, by the subsequent year's member contributions.

The Water Works's property and casualty contributions to the risk pool are recorded as disbursements from its operating funds at the time of payment to the risk pool. The Water Works's contribution to the Pool for the year ended June 30, 2010 was \$44,973

The Pool uses reinsurance and excess risk-sharing agreements to reduce its exposure to large losses. The Pool retains general, automobile, and public officials' liability risks up to \$350,000 per claim. Claims exceeding \$350,000 are reinsured in an amount not to exceed \$2,650,000 per claim and \$10,000,000 in aggregate per year. For members requiring specific coverage from \$3,000,000 to \$10,000,000, such excess coverage is also reinsured. Property and automobile physical damage risks are retained by the Pool up to \$150,000 each occurrence, each location, with excess coverage reinsured by The Travelers Insurance Company.

The Pool's intergovernmental contract with its members provides that in the event a casualty claim or series of claims exceeds the amount of risk-sharing protection provided by the member's risk-sharing certificate, or in the event that a series of casualty claims exhausts total member's equity plus any reinsurance and any excess risk-sharing recoveries, then payment of such claims shall be the obligation of the respective individual member. As of June 30, 2010, settled claims have not exceeded the risk pool or reinsurance coverage since the Pool's inception.

Members agree to continue membership in the Pool for a period of not less than one full year. After such period, a member who has given 60 days prior written notice may withdraw from the Pool. Upon withdrawal, payments for all casualty claims and claim expenses become the sole responsibility of the withdrawing member, regardless of whether a claim was incurred or reported prior to the member's withdrawal. Members withdrawing within the first six years of membership may receive a partial refund of their casualty capital contributions. If a member withdraws after the sixth year, the member is refunded 100 percent of its casualty capital contribution. However, the refund is reduced by an amount equal to the annual casualty operating contribution which the withdrawing member would have made for the one-year period following withdrawal.

The Water Works also carries insurance purchased from Iowa Municipalities Workers Compensation Association (IMWCA) for coverage associated with workers compensation in the amount of \$1,000,000. The Water Works assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims resulting from this risk have not exceeded insurance coverage in any of the past three fiscal years.

The Water Works purchased coverage from another insurer for employee blanket bond in the amount of \$25,000.

Note 7. Sanitary Sewer Receipts

The Water Works assesses and collects sanitary sewer charges for the City of Knoxville, Iowa. The receipts from collections from customers and remittances to the City of Knoxville are accounted for in the Agency – Sanitary Sewer Receipts Fund.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
NOTES TO FINANCIAL STATEMENTS  
June 30, 2010

Note 8. Operating Lease

The Knoxville Water Works is leasing equipment from Pitney Bowes which expires in fiscal year ending June 30, 2013. The Water Works makes quarterly rental payments of \$1,255. The rental payments disbursed during the year ended June 30, 2010 totaled \$5,019.

Details of the operating lease are as follows:

<u>Year Ending June 30,</u>	<u>Principal</u>
2011	\$ 5,019
2012	5,019
2013	<u>2,509</u>
	<u>\$ 12,547</u>

Note 9. Construction Commitment

The City of Knoxville has approved contracts that include projects that the Water Works will reimburse the City for. These two projects, S. 5<sup>th</sup> Street and Robinson Street, are projects that could total \$537,930, which the Water Works would be obligated to reimburse the city when completed.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
BUDGETARY COMPARISON SCHEDULE OF RECEIPTS, DISBURSEMENTS AND CHANGES IN BALANCES  
BUDGET AND ACTUAL (CASH BASIS) – PROPRIETARY FUNDS  
Required Supplementary Information  
Year Ended June 30, 2010

	Actual	Reclassification and Adjustments	Net	Original and Final Budgeted Amounts	Budget to Net Variance
Receipts:					
Water:					
Use of money and property	\$ 23,990	\$ -	\$ 23,990	\$ 35,000	\$ (11,010)
Charges for services	1,582,814	-	1,582,814	1,716,500	(133,686)
Miscellaneous	62,628	(12,650)	49,978	52,000	(2,022)
Total receipts	<u>1,669,432</u>	<u>(12,650)</u>	<u>1,656,782</u>	<u>1,803,500</u>	<u>(146,718)</u>
Disbursements:					
Business type activities:					
Water	<u>1,275,841</u>	<u>(13,895)</u>	<u>1,261,946</u>	<u>1,935,500</u>	<u>673,554</u>
Excess (deficiency) of receipts over (under) disbursements	393,591	1,245	394,836	(132,000)	<u>\$ 526,836</u>
Balance beginning of year	<u>1,153,189</u>	<u>(39,449)</u>	<u>1,113,740</u>	<u>874,832</u>	
Balance end of year	<u>\$ 1,546,780</u>	<u>\$ (38,204)</u>	<u>\$ 1,508,576</u>	<u>\$ 742,832</u>	

See accompanying independent auditor's report.



CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
NOTES TO REQUIRED SUPPLEMENTARY INFORMATION – BUDGETARY REPORTING  
June 30, 2010

The budgetary comparison is presented as Required Supplementary Information in accordance with Government Accounting Standards Board Statement No. 41 for governments with significant budgeting perspective differences resulting from not being able to present comparisons for the General Fund.

In accordance with the Code of Iowa, the Board of Trustees annually adopts a budget on the cash basis following required public notice and hearing for all funds except Fiduciary Funds. The annual budget may be amended during the year utilizing similar statutorily prescribed procedures. Encumbrances are not recognized on the cash basis budget and appropriations lapse at year end.

Formal and legal budgetary control is based upon nine major classes of disbursements known as functions, not by fund or fund type. These nine functions are: public safety, public works, health and social services, culture and recreation, community and economic development, general government, debt service, capital projects and business type activities. Function disbursements required to be budgeted include disbursements for the Enterprise Funds. Although the budgeted document presents function disbursements by fund, the legal level of control is at the aggregated function level, not by fund.

INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING  
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS  
PERFORMED IN ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS

To the Board of Trustees  
City of Knoxville Municipal Water Works Fund  
Knoxville, Iowa

We have audited the accompanying financial statements of the business type activities, each major fund and the aggregate remaining fund information of the City of Knoxville Municipal Water Works Fund as of and for the year ended June 30, 2010, which collectively comprise the Water Works basic financial statements listed in the table of contents and have issued our report thereon dated August 16, 2010. Our report expressed unqualified opinions on the financial statements which were prepared in conformity with an other comprehensive basis of accounting. We conducted our audit in accordance with U.S. generally accepted auditing standards and the standards applicable to financial audits contained in Governmental Auditing Standards, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit we considered City of Knoxville Water Works internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not the purpose of expressing an opinion on the effectiveness of City of Knoxville Water Works internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of City of Knoxville Water Works internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses and, therefore, there can be no assurance all deficiencies or material weaknesses have been identified. However, as described in the accompanying Schedule of Findings, we identified a deficiency in internal control over financial reporting that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility a material misstatement of Knoxville Water Works financial statements will not be prevented or detected and corrected on a timely basis. We consider the deficiency described in Part I of the accompanying Schedule of Findings as item I-A-10 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether City of Knoxville Municipal Water Works Funds financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

Comments involving statutory and other legal matters about the Water Works's operations for the year ended June 30, 2010 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the Water Works. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

City of Knoxville Water Works responses to findings identified in our audit are described in the accompanying Schedule of Findings. While we have expressed our conclusions on the Organization's responses, we did not audit City of Knoxville Water Works responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of the City of Knoxville Water Works and other parties to whom the City of Knoxville Water Works may report. This report is not intended to be and should not be used by anyone other than the specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of the City of Knoxville Water Works during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

Knoxville, Iowa  
August 16, 2010

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
SCHEDULE OF FINDINGS  
Year Ended June 30, 2010

Part I: Findings Related to the Financial Statements:

Instances of Non-Compliance:

No matters were noted.

Internal Control Deficiencies:

I-A-10 Segregation of Duties - One important aspect of internal control is the segregation of duties among employees to prevent an individual employee from handling duties which are incompatible. With only two individuals in the office, it is necessary on numerous occasions for the same individual to prepare water billings, receive cash, prepare the deposits, post collections to customer accounts, and prepare payroll and disbursements.

Recommendation - We realize that with a limited number of office employees, segregation of duties is difficult. However, we believe the Board should be aware of the situation and, as conditions change, review its operating procedures to obtain the maximum internal control possible under the circumstances.

Response - We are aware of the situation, however with the current staffing we do not believe there is a practical way of improving the segregation of duties.

Conclusion - Response accepted.

CITY OF KNOXVILLE  
MUNICIPAL WATER WORKS FUND  
SCHEDULE OF FINDINGS  
Year Ended June 30, 2010

Part II: Other Findings Related to Required Statutory Reporting:

- 1) Certified Budget - Disbursements during the year ended June 30, 2010 did not exceed the amount budgeted in the business type activities function.
- 2) Questionable Disbursements - We noted no disbursements that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.
- 3) Travel Expense - No disbursements of Water Works's money for travel expenses of spouses of Water Works's officials or employees were noted.
- 4) Business Transactions – No business transactions between Water Works and Water Works's officials or employees are noted.
- 5) Bond Coverage - Surety bond coverage of Water Works's officials and employees is in accordance with statutory provisions. The Board should continue to review the amount of coverage annually to insure that the coverage remains adequate for current operations.
- 6) Board Minutes - No transactions were found that we believe should have been approved in the Board minutes but were not.
- 7) Deposits and Investments - We noted no instances of noncompliance with the deposit and investment provision of Chapter 12B and 12C of the Code of Iowa and the Water Works's investment policy.

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